



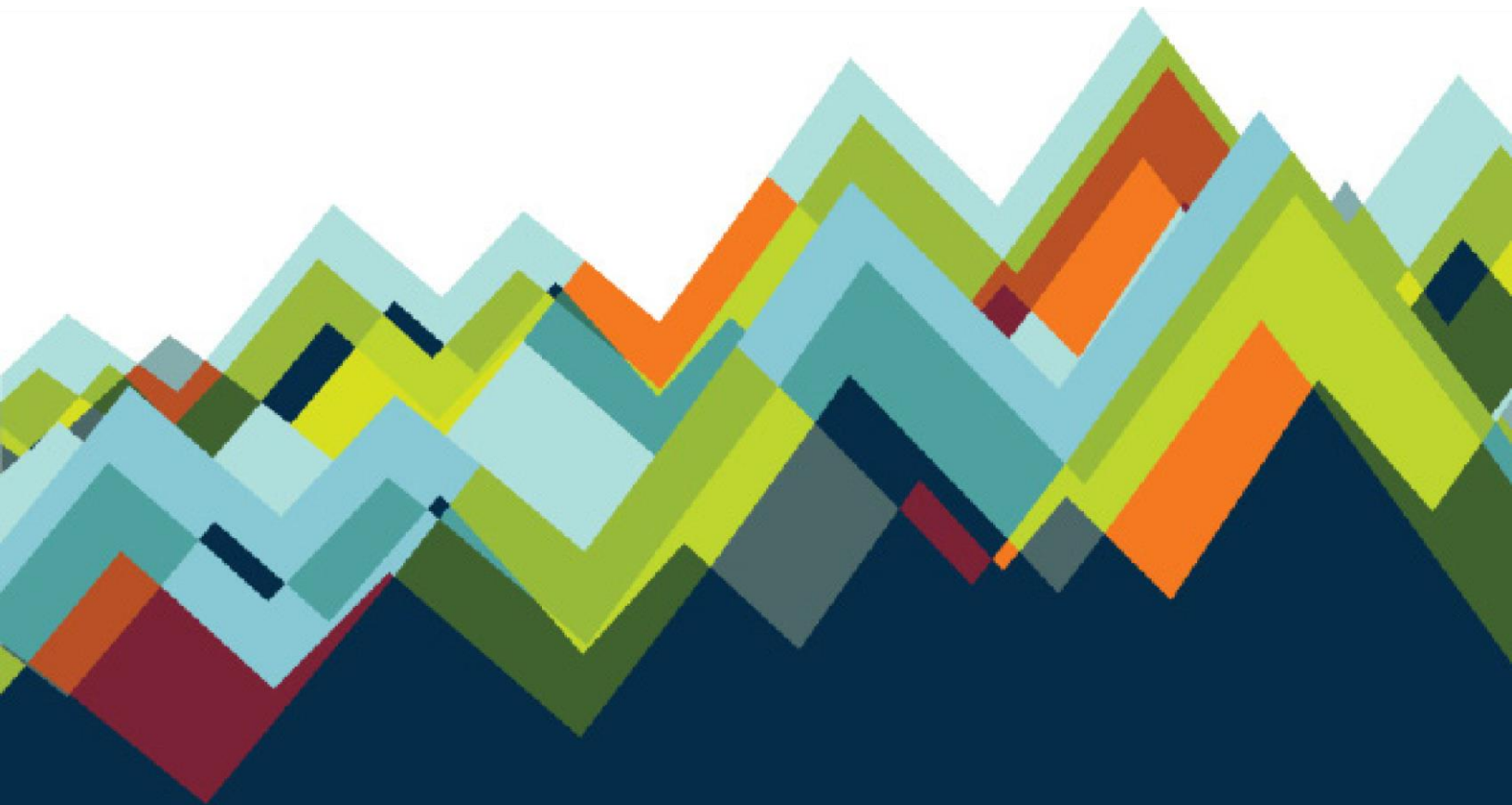
British Columbia  
Securities Commission

# Capital Raising for

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## Cooperative Associations

British Columbia Securities Commission



This Guide is published by the British Columbia Securities Commission, the independent Crown agency responsible for regulating BC's capital markets.

The information in this Guide is for educational purposes only and does not constitute legal advice.

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# INTRODUCTION

In BC, a co-operative association (co-op) is an organization that is owned and operated by people who use and benefit from its services. The owners and operators, called members, may contribute to the capital of a co-op by:

- purchasing *membership shares* as a condition of admission as a member
- purchasing *investment shares* if their issuance is authorized by the memorandum incorporating the co-op

However, non-members may also purchase investment shares if permitted by the memorandum incorporating the co-op.

This Guide is for co-ops that want to raise money by issuing membership shares or investment shares. It explains some of the securities laws that apply to co-ops seeking to raise capital.

## SECURITIES LAW – WHAT ARE THE KEY

There are two key principles of securities law:

1. **Prospectus Requirement:** Every issuer that distributes previously unissued securities (such as bonds or shares) must file a prospectus with the British Columbia Securities Commission (the Commission) and obtain a receipt. A prospectus is a comprehensive document that discloses all material information about the issuer and the securities being sold.
2. **Registration Requirement:** Every person who is in the business of selling securities, in the business of advising another person on the purchase or sale of securities, or is operating an investment fund, must be registered with the Commission. Registered firms and individuals must comply with certain obligations. For example, registered firms and individuals are subject to requirements relating to handling conflicts of interest and assessing the suitability of investments for their clients.

However, there are exemptions available from the prospectus and registration requirements, and a co-op can use an exemption if it can meet the conditions of that exemption. Exemptions generally reduce the time, effort and expense of raising capital. The Commission provides exemptions in various circumstances, such as situations where the purchaser is sophisticated or otherwise able to protect themselves or withstand the loss, or where the purchaser has a close relationship with the organization that would enable the purchaser to access material information about the business.

# WHAT ARE THE PROSPECTUS EXEMPTIONS COMMONLY AVAILABLE TO CO-OPS?

The prospectus requirement in securities law helps ensure that investors have sufficient information to make informed investment decisions. However, there are several exemptions from the prospectus requirements that co-ops may be able to use to issue membership shares and investment shares to members and investors.

This section describes the most common exemptions used by co-ops. A co-op may use a combination of exemptions when raising capital, so long as the co-op meets the requirements of each exemption used. It is the responsibility of the co-op and its directors and officers to understand their obligations under securities law and ensure that the requirements of the exemption being used are met; outsourcing certain compliance functions does not relieve the co-op and its directors and officers of that responsibility.

## 1. Co-op exemption

One of the most commonly relied upon exemptions for co-ops incorporated under the *Cooperative Association Act* (BC) is the co-op exemption in BC Instrument 45-530 *Exemptions for Securities Issued by a Cooperative Association*. A co-op may issue membership shares and investment shares to its members and prospective members under this exemption if the co-op meets the conditions to use the exemption.

A co-op can issue *membership shares* without a prospectus if the purchaser's cumulative investment will not exceed \$10,000.

A co-op can issue *investment shares* without a prospectus if:

- the purchaser's cumulative investment will not exceed \$10,000
- the purchaser has been a member for at least 12 months or since the inception of the co-op, and
- the co-op has fewer than 150 members in BC, excluding full-time co-op employees

A co-op is not required to file a report of exempt distribution to sell shares under the co-op exemption.

### **\$10,000 cumulative investment limit**

This condition requires that the purchaser's cumulative investment does not exceed \$10,000. That is, the cost of the membership or investment shares to be purchased plus the previous cost<sup>1</sup> of any membership and investment shares owned by the member must be less than \$10,000.

It is the responsibility of the co-op to confirm with the purchaser that the purchaser will not end up investing more than \$10,000 in the co-op as a result of the purchase. The co-op must do so by obtaining

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<sup>1</sup> The cost of patronage and dividend shares is not included when calculating the member's cumulative investment.

a written declaration from the purchaser confirming the amount the purchaser paid for all of the membership and investment shares the purchaser already owns.

If the purchaser has already invested more than \$10,000 in the co-op, for example, by having relied in full or part on other exemptions, then the co-op cannot sell any more securities to the purchaser under the co-op exemption. The co-op could sell securities to that member if the co-op and the member meet the conditions for a different prospectus exemption.

This condition does not mean that every member of the co-op must remain below the \$10,000 cumulative investment limit. A co-op could sell shares to a purchaser using the co-op exemption (provided they will have invested less than \$10,000 cumulatively in the co-op after the purchase and meet all the other conditions) even if another member has invested more than \$10,000 under another prospectus exemption, such as the accredited investor exemption.

### **12 month membership requirement**

A co-op cannot issue investment shares to a purchaser under this exemption unless they have been a member for at least 12 months. However, if the co-op is less than 12 months old, the co-op can issue investment shares to a purchaser who has been a member since the inception of the co-op.

This does not mean a co-op must wait 12 months before issuing investment shares; a co-op may issue investment shares as long as it can rely on another prospectus exemption.

### **150 member limit**

A co-op may rely on this exemption to sell investment shares to its members at any time when it has fewer than 150 members. Previous sales under the exemption are not subsequently invalidated if the co-op grows to more than 150 members at a later time, but at that later time the co-op would no longer be able to rely on the exemption to issue investment shares. The co-op may, however, at that later time:

- issue *membership shares* to new members under the co-op exemption or another exemption if it is able to satisfy the conditions of the exemption to be relied upon
- issue *investment shares* to members or non-members using another prospectus exemption

## **2. Private issuer exemption**

A co-op is a “private issuer” if it has fewer than 50 security holders (excluding employees and former employees) and its memorandum (or security holders’ agreement) contains restrictions on the transfer of securities. This exemption allows a co-op to raise any amount of money from the following types of people:

- directors, officers and employees
- family members of directors or senior officers
- close personal friends of directors or senior officers
- business associates of directors or senior officers
- accredited investors

A private issuer is not required to file a report of exempt distribution to sell securities under this exemption.

As long as a co-op continues to meet the definition of a private issuer, it can raise money from the people listed above. Similar to the co-op exemption, the fact that the co-op has more than 50 members later does not invalidate the exemption previously used, but it will no longer be able to rely on the private issuer exemption going forward.

### 3. Offering memorandum exemption

Co-ops may also raise any amount of money from anyone using the offering memorandum exemption (OM exemption). An offering memorandum is a disclosure document that is shorter and less detailed than a prospectus. It must describe the co-op's business and management, including the relevant risks, and explain how the co-op will use the money it raises. The co-op must include audited annual financial statements in the offering memorandum.

The co-op must also give any purchaser under the OM exemption a risk acknowledgement form and make sure the purchaser signs it.

Unlike the process of becoming a reporting issuer in which a prospectus must be receipted by the Commission, using an offering memorandum does not make a co-op a reporting issuer and does not require a receipt from the Commission or any other review. However, the offering memorandum must be filed with the Commission within 10 days after the securities are sold<sup>2</sup> under the OM exemption. The co-op will also need to file a report of exempt distribution with the Commission within 10 days of the securities being sold.

Use of the OM exemption is not limited to raising funds for a particular project. Co-ops can use an offering memorandum to raise funds on an on-going basis so long as the information in the offering memorandum is true and up-to-date. An offering memorandum will have to be updated before it can be used if the certificate<sup>3</sup> ceases to be true or the financial statements it must contain become outdated. If a co-op is not using the offering memorandum to raise funds, there is no obligation to update the financial statements.

**Additional reading:** If your co-op is considering using the OM exemption, you should read [Multilateral CSA Staff Notice 45-309 Guidance for Preparing and Filing an Offering Memorandum under National Instrument 45-106 Prospectus and Registration Exemptions](#). This document sets out common deficiencies when using offering memorandums.

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<sup>2</sup> If the issuer is conducting multiple closings, the offering memorandum must be filed on or before the 10<sup>th</sup> day after the first closing. Once the offering memorandum has been filed, there is no need to file it again after subsequent closings, unless there is a change to the marketing materials.

<sup>3</sup> The offering memorandum must contain a certificate that states: "**This offering memorandum does not contain a misrepresentation.**" A misrepresentation is an untrue statement of a material fact or an omission of a material fact.

## 4. Other exemptions

Some other exemptions that co-ops may rely on include:

- accredited investor exemption – allows co-ops to raise money from investors who meet specific minimum annual income and net worth levels
- friends, family and business associate exemption – allows co-ops to raise money from investors who are members of the immediate families, close friends and close business associates of a director or an executive officer
- employee, executive officer, director and consultant exemption – allows co-ops to raise money from their employees, executive officers, directors and consultants
- minimum investment of \$150,000 exemption – allows co-ops to raise money from other companies (not individuals) investing at least \$150,000

The use of some prospectus exemptions – including the accredited investor exemption, the friends, family and business associate exemption and the minimum investment of \$150,000 exemption – would require the co-op to file a report of exempt distribution within 10 days after the securities are sold.

**Additional reading:** For more information on these exemptions, you should read [Guide on Capital Raising for Small Business](#).

## 5. Discretionary relief

If a co-op is unable to rely on an exemption such as the co-op exemption, because it is unable to meet one of the requirements, the co-op may be able to apply to the Commission for exemptive relief. The co-op must be able to demonstrate that there is no investor protection concern arising from distributing its shares without a prospectus. If your co-op is considering making an exemptive relief application, you may wish to visit the [Applying for an Exemption](#) page on the Commission's website, and to search our exemptive relief decisions using the Commission's e-services research tool to see if we have granted exemptions in similar circumstances before. The co-op could also consult with a lawyer about the merits of the application.

# WHAT SHOULD CO-OPS KNOW ABOUT THE REGISTRATION REQUIREMENT?

Securities law has a registration requirement to help ensure that persons in the business of selling securities are required to know their clients and to determine whether the investment is suitable for them. For example, a registered dealer can provide advice to their clients about the risks, RRSP eligibility or tax advantages of an investment, as well as whether that investment is suitable for them based on these and other factors.

We amended the co-op exemption to remove the dealer registration exemptions because a co-op will generally be exempt from registering as a dealer if it is not in the business of trading.

A co-op's officers, directors and employees who are involved in raising money through the sale of securities will generally not be subject to the registration requirement if they:

- are not principally employed to sell the co-op's securities
- do not spend most of their time selling the co-op's securities
- are not paid to sell the co-op's securities, and
- are not acting in a manner similar to a "finder" for investments in the co-op's securities

However, a co-op would need to register as a dealer if it is in the business of selling securities, including co-op shares. This may also apply separately to the co-op's officers, directors or employees.

**Additional reading:** Further guidance on when firms are in the business of trading can be found in [Companion Policy 31-103CP Registration Requirements, Exemptions and Ongoing Registrant Obligations](#).

A co-op will also need investment fund manager registration if it is directing or managing the business, operations or affairs of an investment fund. For example, a non-redeemable investment fund is an issuer whose primary purpose is to invest money provided by its security holders and that does not invest for the purpose of exercising control of an issuer. If a co-op invests money provided by its security holders in other businesses as a passive investor, it may be directing or managing an investment fund which would require an investment fund manager registration. Whether a co-op is an investment fund depends on the facts and must be assessed on a case-by-case basis.

## INVESTOR EXPECTATIONS

Read our [Guide to Investing: The Private Placement Market for Retail Investors](#) to understand the level of information we encourage private investors to seek when investing in the exempt market. This and other useful guides are available at [www.investright.org](http://www.investright.org).

Some of the information we suggest investors seek before investing includes:

- the full legal names of directors and officers so that they can conduct background checks
- a comprehensive set of financial statements showing the financial position, operating history, and cash flow of the business (ideally, these should be audited)
- the purpose for which the business is raising money and whether the planned fundraising will provide sufficient funds, and a business plan including how the business will make money and within what time period

Your co-op should be aware that some investors may request this type of information. For example, a co-op in the business of investing money provided by its security holders may have investors ask for information to enable them to understand the co-op's underlying investments.



## FOR MORE INFORMATION, CONTACT BCSC INQUIRIES

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